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The Cuban Debt Proposal: The Soviet Angle

Summary

Over the last six months Cuban leader Fidel Castro has intensified his longstanding campaign to encourage Third World leaders to cancel their foreign debts to Western lenders. Although the campaign has yet to catch fire and seems unlikely to win over many LDCs, Castro almost certainly will continue to pursue it to further his own and Soviet goals. Castro's effort offers some opportunities to the USSR, and the Kremlin has provided modest rhetorical support. The Soviets almost certainly welcome the building up of resentment in LDCs against Western lenders. Such resentment might generally shore up Moscow's position as a Third World benefactor and, in individual countries, the USSR may be able to capitalize on the political instability that may result. At the same time, we believe the Cuban leader has been acting on his own initiative, despite some allegations that the USSR has pushed Castro to trigger the renewed rhetoric. While Havana and Moscow have mutual interests and goals in the campaign, the Soviets probably do not want it to actually succeed for fear that a massive debt cancellation throughout Latin America could disrupt the global markets on which they and their East European allies depend, provide an

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unwelcome example to the destitute Marxist clients that owe them money, and affect their own profitable dealings with LDCs. Tactically, the Soviets have been embarrassed by Castro's rivalry over leadership on the debt issue with the new Peruvian President, Alan Garcia, whom they have been courting. Over the next few months, the USSR probably will continue to press for global talks on the debt crisis so that it can push its own anti-Western views, but will probably continue to avoid embracing Castro's specific proposal. [redacted]

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The Castro Proposal

1. Over the last six months, Cuban leader Fidel Castro has intensified his longstanding campaign to encourage Third World leaders to repudiate the debts they owe to Western lenders. At times he has called for a moratorium; more frequently he has advocated permanent cancellation. He initially focused on the debts owed by Latin American countries, but judging from his recent speeches and Cuba's focus on the topic at the September 1985 Non-Aligned Movement (NAM) ministerial meeting he is seeking to broaden the campaign to all less developed countries (LDCs). Castro has lambasted the International Monetary Fund (describing it as a "new form of economic colonialism"), US-based multinational banks, and the US and other Western governments. From 30 July to 4 August Castro presided over a "Latin American and Caribbean Meeting on the Foreign Debt" in Havana, and he has peddled his line to smaller Latin American conferences as well. By involving various groups--including the media, labor and political leaders, and students--Castro hopes to create a series of broadly-based fronts that will persuade each Latin American government to repudiate its debt [redacted]

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Moscow and Havana's Parallel Interests

2. Several factors suggest that the Cubans and Soviets are working together to exploit the debt question. The USSR generally tries to gain maximum payoff from its support for Third World economic grievances, usually by contrasting the "pernicious" behavior of Western-based multinational corporations with the Soviet Bloc's "disinterested" support for LDC demands such as those for a "New International Economic Order" (NIEO). Articles by specialists and in the press show that the Soviets recognize the large reservoir of Latin American resentment against US banks, the IMF, and other Western creditors that existed well before Castro embarked on his campaign; Moscow

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undoubtedly sees the LDC debt issue as a lucrative area to exploit. Both Moscow and Havana have portrayed the debt as a political (not economic) issue requiring a political solution-- either outright cancellation or a debt moratorium. [redacted]

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3. The USSR has demonstrated its common interests with Cuba on the debt issue in other ways:

- Soviet academics seem to have stepped up their study of the LDC debt issue, presumably at the leadership's encouragement. [redacted]

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[redacted] The head of the USSR's Latin American Institute publicly claimed in May that his organization's top research topic was Latin American debt.

- The Soviets have flourished before LDC debtors the agreement allowing Peru to repay its debt to the USSR with commodities, contrasting this with the "callousness" of the IMF and Western governments. [redacted]

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[redacted] by allowing Peru to repay its debt with goods rather than cash, the Soviets have gained a tremendous amount of good will that they expect will spill over into political relations. Moscow may consider similar arrangements with other Latin American countries and expects this flexibility to garner good will for the USSR in other geographic regions. [redacted]

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4. The USSR arguably has a strong incentive to use Cuba as a surrogate rather than directly attack Western banks and governments. Moscow's longstanding support for the economic demands of the more radical members of the Non-Aligned Movement has not generated wide support in the Third World. Since the 1976 UN Conference on Trade and Development (UNCTAD), LDCs generally have become more aware of the Kremlin's paltry economic aid and they have put the USSR in the same category as the West-- attacking both as part of the "industrialized North." Thus, the Soviets probably believe that Castro has more credibility in the Third World, particularly in Latin America, than they. The USSR may have a special incentive to let Castro take the lead in the period leading up to Gorbachev's meeting with President Reagan in order to avoid offending the US. Moscow also would want to avoid giving Western Europe the impression that it is a force for economic chaos since that region is crucial to Soviet interests for both commercial and political reasons. [redacted]

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5. [redacted] Castro's speeches on the debt proposal illustrate the degree to which Cuban and Soviet interests dovetail. In speeches on Latin America's debt, he has

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been careful to protect his benefactor's interests. During the Havana conference the Cuban leader differentiated the USSR from Western creditors, making clear he regarded the latter as the sole cause of the LDC crisis. Cuban officials at the conference characterized the debt issue as a Third World problem and noted that the USSR--a "Second World" power--bears no responsibility for the crisis. Castro also has said that any agreement reached by debtor nations in Latin America must have "the support of the USSR and other socialist countries," [redacted]

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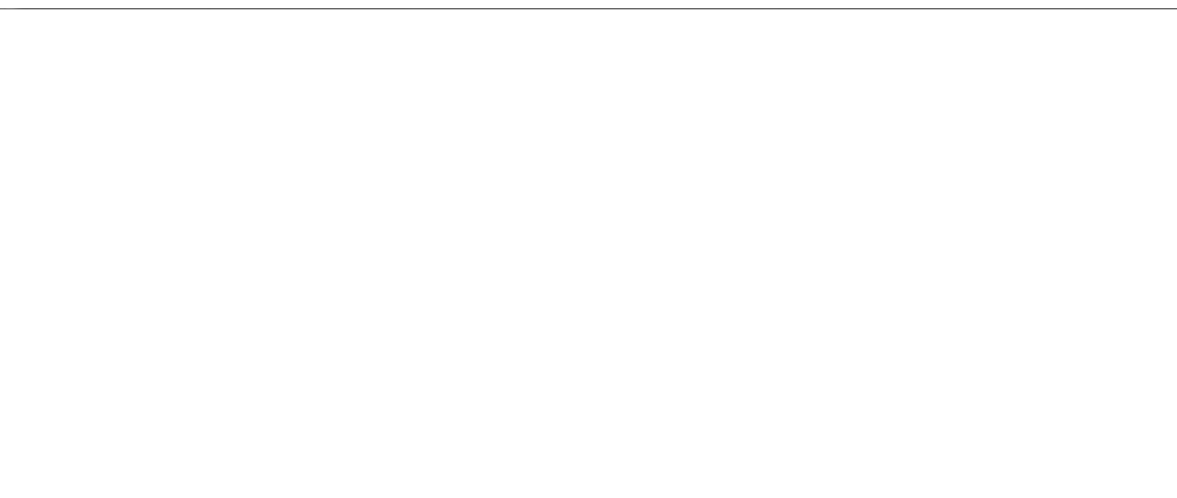
[redacted] Castro has challenged the US to pay off Latin America's debt by reducing its military expenditures by 12 percent--not surprisingly, he does not mention Soviet military spending--and his definition of certain debts as "illegal" protects Soviet interests. In an interview with a Brazilian newspaper last June, he declared:

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"An illegal debt is made up of usurious interest rates, which does not mean that we believe in the Moslem concept that no interest should be charged. In our opinion, interest rates higher than 8 percent a year (for) contracts signed at the time when the market was satisfied with just 6 percent constitute a . . . clearly usurious rate, considering that the economies of the creditors have to deal with inflation rates of less than 4 percent."

Since the USSR charges some interest for its loans--but well below the rate charged by Western creditors and almost always under 8 percent--Castro seems to absolve Moscow of responsibility for the debt crisis. [redacted]

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Divergencies Between Moscow and Havana on the Debt Issue

7. Although Soviet and Cuban interests on LDC debt closely coincide, several differences in approach and emphasis have

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emerged over the course of this past summer. These differences probably reflect, in large part, Moscow's unease over the consequences that a large-scale LDC debt annulment would have on its own economic interests. [redacted]

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8. Soviet rhetorical support for the Cuban initiative has been surprisingly lukewarm, as exemplified by an Izvestiya article by Aleksandr Bovin, an authoritative commentator, in early July. Beyond claiming that Castro has "elicited a great response in Latin America," the closest Bovin comes to endorsing the Cuban proposal is to say "it can be seen as the only realistic one." Moreover, he concludes his commentary with a call to "avert a catastrophe which could cause international economic confusion" and with the pale observation that "the crisis continues. Another TASS report on a meeting of journalists in Havana merely quotes Castro about the need for a debt moratorium and also fails to explicitly endorse it. In his statement on 24 September to the UN General Assembly, Soviet Foreign Minister Shevardnadze described the proposal blandly without embracing it: "Cuba and some other member states of the United Nations propose ways of solving the problem of financial indebtedness."

9. Although the Soviets have not completely backed the Cuban proposal, they have given full support to the Third World's "struggle" against the "unjust" capitalistic economic system. In late October, the Warsaw Pact states declared:

"There is an urgent need for the settlement of the problem of the developing countries' external debt, which is one of the burdensome consequences of colonialism . . . The socialist states advocate . . . the speediest start of specific businesslike negotiations within the UN framework and with the participation of all states with a view to the global and just settlement of the most important international economic problems including . . . external indebtedness."

Moscow's implicit message seems to be that it would like to capitalize on any momentum the Cuban President may have created on the debt issue, but only through global talks that would include the Soviet Bloc rather than through unilateral Third World action--and not necessarily for the purpose of achieving Castro's stated goal, large-scale debt repudiation. [redacted]

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10. The USSR's mildness on the issue--compared to Castro's inflammatory rhetoric--may reflect not so much a lack of enthusiasm as a desire to have Castro out on front on the issue and to obscure its own connection with the campaign. Moreover, the Soviets almost certainly recognize that their record on economic development issues puts them in no position to take the lead on Third World issues. Moscow's pragmatism also is in line

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with its cautious overall approach to the Third World's other economic demands (see Appendix). [redacted]

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11. In contrast to Moscow's reserved and belated reaction to the possibility of LDC debt repudiation, Castro's campaign has much deeper roots. The Cuban leader has a long history as a vocal supporter for Third World causes, particularly LDC demands that the "North" redistribute massive economic resources to the "South." His rhetoric on the debt issue goes back at least to a 1979 speech at the UN General Assembly. The present debt campaign is an expression of his self-portrayal as the Third World's most important spokesman against Western economic "imperialism"--as exemplified during his chairmanship of the NAM from 1979-82. It is also a natural continuation of his decades-old vendetta against the United States. Castro's outspokenness on the debt issue may even increase if he decides, as rumored, to cede some of his day-to-day governmental responsibilities to his brother Raul. [redacted]

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12. The tarnishing of Castro's image in recent years as the "natural leader" of all LDCs probably has prompted the Cuban President to try to regain the initiative. He almost certainly is eager to demonstrate that he can still exert considerable influence on the international stage despite the overthrow of the pro-Cuban regime in Grenada and the setbacks of the Central American insurgents. He probably is also trying to erase his image as a slavish Soviet mouthpiece. Thus, Castro probably sees the debt issue as a key to winning renewed recognition and acceptability in the Third World and ending his diplomatic isolation in the hemisphere. [redacted]

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13. Castro also may be trying to use the debt campaign to distract the Cuban population's attention from economic problems at home and its resentment of the costs of Third World involvement. Focusing on Latin America's financial bind allows Castro to deflect some domestic criticism of Cuba's own economic ills. (At the same time, however, Castro also risks raising in people's minds the issue of Cuba's own debt to the USSR.) [redacted]

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14. A third, probably more important, audience to whom Castro may be playing is the USSR. He may be using the debt campaign as one among several means of encouraging Moscow to maintain a high level of political and financial support. Castro probably is making the claim to his Soviet patrons that the campaign helps them because it puts the US more on the defensive in the Western Hemisphere and increases animosity between the US and Latin America. [redacted]

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15. Several pieces of evidence point to the contrast between Castro's leading role on the debt campaign and Moscow's relative passivity:

- Castro's self-proclaimed leadership on the debt issue provoked an angry exchange with Alan Garcia, Peru's newly-elected President, in whom the Soviets have placed great hopes because of his promise to be more "even-handed" toward the two superpowers than his predecessor. Garcia called Castro's proposal inapplicable to any Latin country other than Cuba, and Castro sent an insulting "congratulatory" message to Garcia on his election, attacking Peru for its high rates of illiteracy and infant mortality and its social inequalities. This episode suggests that the Soviets probably were taken by surprise and could not control the tactical moves Castro chose to use for his campaign.
- The contrast in tone between Castro's speeches and Soviet writings suggests that the Cuban leader is much more committed personally to debt repudiation than the Soviets. This is, in fact, precisely the sort of grandstand issue on which Castro seems to thrive. His rhetoric on the need for debt repudiation has been punctuated with bombast and hyperbole; in contrast to his emotional appeals--replete with allusions to the world being in the midst of World War III because of LDCs' massive debts--Soviet writings seem coolly analytical, almost cold-blooded.
- Castro seems more willing than Moscow would be to take radical action to support his proposal.

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Castro's willingness to work for the restructuring of regional governments stands in contrast to the Soviets' more cautious and long-term approach.

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How Would LDC Debt Repudiation Affect the USSR?

16. Economic effects. A foreign debt cancellation by all or most major LDC debtors--or even just Latin American debtors--could very well lead to the collapse of the international financial order, harming not only Western economic interests but Soviet interests as well and short-circuiting Gorbachev's ambitious plans to improve the domestic economy. Soviet economic

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planners depend on the smooth functioning of commercial and financial markets because they import significant quantities of Western technology and agricultural products and rely on overseas export markets to earn hard currency. According to Soviet and Western data, the USSR's hard currency trade turnover has ballooned (in nominal dollars) from \$2 billion in 1960 to an estimated \$59 billion in 1984, and its hard currency debt has grown as well; from 1971 to 1984, Soviet commercial debt rose from \$0.4 billion to \$11.3 billion and government-backed debt rose from \$1.4 billion to \$8.9 billion. [REDACTED]

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17. Large-scale debt repudiation could also hurt Soviet economic interests in other ways:

- It could put pressure on Moscow to step in with alternative financing for LDCs; although the Soviets almost certainly would resist this pressure, this would cost them some political good will in the Third World.
- If LDCs repudiated their past obligations, they almost certainly would find it next to impossible to borrow additional amounts. This would probably cause them to significantly scale back economic activity, including the production of export goods. Moscow could then have trouble persuading LDCs to sign commercial agreements in which Moscow could receive payment in commodities useful to its economy.
- Reduced economic capabilities among the more affluent LDCs also could hurt Soviet efforts to establish lucrative joint venture projects there involving third-country partners (either Western countries or other developing countries.)
- If the world's financial markets were plunged into chaos, Eastern Europe would also face serious economic problems, forcing an increase in the level of required Soviet economic aid. [REDACTED]

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18. In addition, Moscow must calculate the effect of Castro's campaign on Soviet Third World client states--that is, whether debt cancellation by non-Communist LDCs would induce countries like Cuba, Ethiopia, and Vietnam to argue for the annulment of their own obligations. Although Castro has targetted his rhetoric against Latin America's debts, Soviet economic planners could fear that a decision by many LDCs to repudiate debts could have an impact on Soviet political influence. Moscow probably is realistic enough to realize that this "demonstration effect" is quite unlikely to actually hurt its economic interests in the foreseeable future. Most of the clients with large debts to the USSR have negligible financial resources, and the Kremlin almost certainly doubts that these

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countries will ever repay these debts in full. Even without Castro's prodding, some of Moscow's very poor clients could, in effect, default on their debts to the USSR. Nevertheless, keeping these debts on the books may enhance Soviet political leverage over these clients and lets them know that Moscow expects at least partial repayment some time in the future. [redacted]

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19. Practically speaking, however, the Kremlin probably is not overly concerned about the possibility of economic fallout from Castro's proposals because it almost certainly recognizes that the Cuban President has virtually no chance of actually convincing the vast majority of non-Communist LDCs to cancel their debts. Soviet economic planners probably realize that none of these countries can afford to alienate their creditors since that would lock them out of additional credits or rescheduling agreements. Thus, the Soviets probably believe that the economic risks of encouraging the Cuban campaign are minimal. [redacted]

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20. Furthermore, the Cubans labor under a considerable handicap that increases Moscow's confidence that their debt proposal probably will never succeed--namely, the widespread and correct impression in Latin America that Castro is in no position to give lectures about other countries' debts. During July and August, at the height of Castro's campaign, several Latin leaders spoke out against the hypocrisy of Cuba advocating debt repudiation when it receives over \$4 billion annually in Soviet economic assistance. Even though this aid permits Cuba to accrue only modest debts to Western governments and banks, Castro has rescheduled his Western official and commercial debts (in fact, once again last July). And Cuba has asked for terms at least as favorable as those the IMF grants to other Latin American countries. Regional leaders consequently have voiced their opposition to Castro's initiatives on these grounds. On 10 August, Venezuelan President Lusinchi said:

"I am not in agreement with [the Cuban initiative]. I don't wish to enter into a public debate with a head of state such as Dr. Castro, who holds to an interpretation of this issue that I do not share . . . It occurs to me to ask . . . what were the refinancing terms for Cuba's debt with the so-called Paris Club and with the USSR and other socialist countries? I have my approaches to the debt, which were expressed in [several other] Latin American declarations. . ."

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[redacted] Mexico, the Third World's second largest debtor, refused to send any delegates to Castro's 30 July debt conference. Peru's President Garcia has opposed Castro's proposals for the same reasons as Mexico. In late September,

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Castro tried to evade questions posed at a Havana youth meeting and press conference about the refinancing of Cuba's own debt and Moscow's preferential treatment of Havana. [REDACTED]

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21. Political effects. In contrast to the negative potential economic effects of a large-scale LDC debt cancellation on Soviet interests, the USSR probably anticipates mostly political advantages in having Castro spout support for--but not achieve--his plan. By agitating on the issue, Moscow and Havana probably believe they can increase pressure on the Third World to "stand up to" the IMF, Western banks, and Western governments. Inflicting financial strain on the IMF and Western banks (up to a point)--and increasing Western diplomatic defensiveness on the LDC debt issue--are probably in Moscow's interest. Because even moderate Latin American leaders believe the region's \$360-billion debt is unbearable, the Soviets and Cubans almost certainly see this issue as a key to exacerbating problems between the US and the Latin Americans and insinuating themselves with a broader spectrum of political opinion than the radical parties that Moscow ordinarily courts. The Kremlin probably also sees the debt problem as a ready-made issue particularly useful to radical parties in Latin America, including the Communists. [REDACTED]

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22. The Kremlin would welcome a movement by LDCs toward more economic cooperation with socialist states. Financially strapped LDCs probably would be tempted to increase their barter trade with the socialist bloc in order to conserve scarce hard currency reserves, even if they do not formally break with the IMF or Western banks. Moscow probably hopes that Castro's campaign will encourage LDCs to feel more aggrieved with the West and to turn increasingly to them for barter and other state-to-state economic accords. In the case of Peru, for example, Moscow has capitalized on the debt crisis by negotiating agreements for repayment in commodities rather than cash. The USSR probably hopes it can strengthen state sector enterprises and weaken private concerns in economically distressed LDCs that turn to Moscow for such help. More generally, to the extent the Soviets can raise political sensitivities throughout Latin America about debt and increase resentment against the IMF, they stand to benefit from any increased political instability that may result. [REDACTED]

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23. At the same time, the impact so far of the Cuban campaign has created an indirect political problem for the Soviets--namely, the continuing isolation of Cuba, probably Moscow's most important client in the Third World, from other Latin American countries. Castro's rhetoric has alienated not only Peru's new president but also the leaders of Venezuela, Mexico, Argentina, and Brazil. Because Castro has set back his own previous efforts to regain respectability for Cuba among its neighbors and reintegrate the country into the Latin American fold by expanding its diplomatic and commercial relations, the

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Soviets probably view the debt campaign in this respect as a marginal political setback. [redacted]

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Conclusion and Outlook

24. Although Castro needed no convincing to begin his debt campaign, Soviet leaders probably let the Cuban leader know he could count on their low-key support since they recognized that he probably would not actually succeed. They probably believed that, on balance, the net political gains of Castro's rhetoric far outweighed the economic risks. In late summer, however, the Soviets undoubtedly recognized the growing rivalry between Castro and Garcia over leadership on the debt question and realized that Castro's posturing could only hurt their efforts to court Peru, their largest arms customer in South America. Viewing this prospect with concern, they probably will try to get Castro to smooth his relations with Garcia. If so, their influence will be severely limited by the Cuban President's egotism and his intense personal interest in the subject. [redacted]

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25. In the next few months, the Soviets probably will continue to keep a low profile, hoping to maximize the political benefits of the campaign and make sure that the prospects for economic fallout from Castro's propaganda blasts remain negligible. While they may very well push for global talks on the debt crisis in order to assert their own views, they will almost certainly avoid embracing Castro's specific proposal. They undoubtedly hope that Castro will realize that outbursts such as those against Garcia hurt not only Moscow's interests in Latin America but Havana's as well. At the same time, the Soviets could step up their modest, behind-the-scenes support, and aid Castro more actively if they feel that anti-debt agitation could help spark political gains in particular Third World countries. [redacted]

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APPENDIXPast Soviet Assessments of LDC Economic Demands

In the 1970s several Third World countries began to make radical demands for a redistribution of global resources from the industrialized "North" to the less developed "South"--a series of proposals collectively known as the New International Economic Order (NIEO). As differences between Soviet and LDC interests began to surface, Moscow's attitudes toward NIEO have gradually shifted away from unqualified support. Moscow has continuously embraced the "anti-imperialist" assertions of NIEO, but has found it harder to swallow some of the Third World's specific demands. Although they have tried to preserve a semblance of anti-Western unity with the Third World (by attacking multi-national corporations and other forms of Western "imperialism"), the Soviets have become more equivocal about NIEO because they no longer believe that a restructuring of the global economy will necessarily redound to their advantage. [REDACTED]

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Between 1974 and 1976 the USSR unreservedly endorsed LDC demands for NIEO, seeing them as a way to exacerbate tensions between the industrialized North and the industrializing South. This was reflected in official speeches, May Day and October Revolution slogans, and specialized articles. Soviet optimism over channeling Third World anti-colonialism to its own purposes faded in 1976 when the LDCs passed a UN General Assembly resolution that held socialist and capitalist countries equally responsible for the Third World's plight and did not address trade discrimination in a way that could help the Soviets. The USSR subsequently voiced official reservations about NIEO proposals. For example, Moscow qualified its support for the creation of a "Global Fund" to aid Third World development because of LDC demands for contributions from all "Northern" countries, regardless of social system. Soviet academic specialists also began to criticize Third World demands for a massive redistribution of global resources on the grounds that, in the absence of substantial domestic reforms, such payments would simply benefit corrupt elites in developing countries. Some Soviet experts even objected to plans to raise raw material prices or create commodity cartels similar to OPEC because of the likelihood of economic injury to the USSR or Eastern Europe. [REDACTED]

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The USSR tried to persuade LDC proponents of NIEO to start emphasizing the evils of trade discrimination generally rather than focus solely on North-South exploitation. To the extent Moscow envisages radical changes in the world economy, it has been careful to stress changes beneficial to its own economy. Thus, the USSR and its East European allies have tried to ensure that any restructuring of the world economy address such problems as Western discrimination against their exports (both discriminatory tariff structures and politically-inspired

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embargoes); unfavorable terms of trade for the East vis-a-vis the West; the effects of Western currency devaluations; and prohibitions against transfers of high-technology Western goods. [REDACTED]

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